

obligation, and NetCo's customers, including ServeCo and the CLECs, will demand a high quality standard. Moreover, current FCC and state regulatory mechanisms to monitor network quality and investment would continue to apply to NetCo. In addition, the development over time of competitive networks should provide NetCo an increasingly strong incentive to keep its network attractive to service providers, whether ServeCo or other CLECs, through additional fiber optic cable, upgraded switches, AIN deployment, and other investments in new technology. Finally, our related state petitions include transitional mechanisms, based on existing price-cap incentives, to assure the continued availability of a basic local exchange service comparable to that offered today.

B. Status of ServeCo as an ILEC Under Section 251(h).

In this petition, LCI has asked the Commission to declare that any RBOC adopting the proposed corporate structure may offer local exchange service through its retail affiliate without concern about being classified as an incumbent LEC under Section 251(h). ^{59/} Incumbent LECs have begun to seek authority from commissions in a number of states to create a "CLEC affiliate" through which they intend to offer local exchange service in competition with themselves, in their own service areas. State commissions have struggled with the notion that the ILEC could create another company to provide local exchange service that would be free from the requirements of Sections 251(c) and 252. ^{60/} The FCC also may soon be asked to resolve the

^{59/} Section 251(h)(1)(B)(ii) of the 1996 Act provides that any "successor or assign" of an incumbent LEC also must be treated as an incumbent LEC. 47 U.S.C. §§ 251(h)(1)(B)(ii). Section 251(h)(2) allows the FCC to classify as an incumbent LEC any LEC that occupies a position in the local market "comparable to" the position held by an incumbent LEC and has "substantially replaced" an incumbent LEC. 47 U.S.C. § 251(h)(2). Whether an entity should be treated as an ILEC is for the Commission to decide.

^{60/} The Texas Commission, for example, has denied GTE a CLEC certificate in its own service area because of these concerns. See *GTE CLEC Certification Order, supra* ("The service area of GTE-CC's COA is limited to the service area of SWBT, Sprint/United, and Centel").

legal and factual question whether the CLEC affiliate of an ILEC should be considered an ILEC under Section 251(h). 61/

An RBOC can avoid the danger of having its interLATA affiliate regulated as an ILEC when it provides local exchange service out of that affiliate by adopting the NetCo/ServeCo structure. Under that structure, the ILEC's Section 251(c) interconnection responsibilities will be met by NetCo, who will have the network facilities to fulfill that role -- and now the reduced conflicts of interest to help it do so on a nondiscriminatory basis.

If LCI's proposal is adopted, the Commission also should rule that ServeCo is not a "successor" or "assign" of the RBOC, and that ServeCo does not occupy a comparable position in the local exchange market, because ServeCo is adequately separated from NetCo and has not assumed the embedded customer base. 62/ Consequently, any RBOC adopting LCI's proposed ServeCo/NetCo structure would not be considered an incumbent LEC within the meaning of

61/ Some might argue that the FCC already has decided that an RBOC's interLATA affiliate cannot become an ILEC under Section 251(h) when it offers local exchange service from the affiliate. This would be incorrect. It is true that the Commission concluded in the Non-Accounting Safeguards proceeding that an RBOC's Section 272 affiliate may provide local service as well as long distance service out of that affiliate. *Non-Accounting Safeguards Order*, 11 FCC Rcd at 22055-56, para. 312. The FCC also held that the mere fact of providing local exchange service in and of itself does not make the affiliate an incumbent LEC within the meaning of Section 251(h). *Id.* The FCC did not determine, however, at what point a transfer of the local exchange functions or customers to the affiliate might trigger a finding that the affiliate should be treated as an ILEC within the meaning of Section 251(h). In fact, the FCC effectively begged the question in the *Non-Accounting Safeguards Order*, by stating only that the interLATA affiliate may offer local exchange service *provided* it does not qualify as an ILEC within the meaning of Section 251(h). *Id.* (emphasis added). Thus, the FCC has correctly left open the question of under what factual circumstances an ILEC affiliate that is providing local exchange service would become an ILEC itself under Section 251(h).

62/ 47 U.S.C. § 251(h)(1), (2). We note, however, that the Commission already has held that if an RBOC were to transfer any of its local exchange facilities to its interLATA affiliate, the affiliate would become an incumbent LEC under Section 251(h)(1) with respect to those facilities. *Non-Accounting Safeguards Order*, 11 FCC Rcd at 22054, para. 309. In any case, we propose in this plan that NetCo be prohibited from transferring network facilities or existing customers to ServeCo, because such transfer would be inconsistent with NetCo's role as carrier's-carrier to the retail operations of ServeCo and others.

Section 251(h). 63/ This would assure RBOCs that their ServeCo affiliates, like other CLECs, would not have to offer the interconnection features mandated under Section 251(c), regardless of the extent to which they are themselves offering local exchange service. 64/

C. Regulation of ServeCo Interstate Services.

One of the premises of LCI's structural approach is that the ServeCo affiliate would be deregulated in all material respects, and would enjoy the same non-dominant carrier status that its competitors have, as it enters the local, intraLATA and interLATA markets. This would ensure that the RBOC can compete on a retail level on an unrestrained, deregulated basis. 65/

Today RBOC interLATA affiliates are subject to more stringent regulation than other service providers in several important respects. For example, such affiliates today would be treated as dominant when they offer bundled packages of local exchange and interLATA (and other) services. 66/ This is appropriate, given that the RBOCs have demonstrated the ability to discriminate in favor of their own local services, and that competitive problems in the local market all the more infect the interLATA market when local and long distance services are sold together in a bundled form.

Moreover, under current regulatory decisions and current case law, although the Commission previously has decided that the stand-alone in-region interstate interLATA services

63/ Of course, the Commission would retain discretion to classify a ServeCo as an ILEC if over time, the NetCo/ServeCo structure does not function as we predict it will.

64/ The end point of our proposal contemplates that NetCo no longer will have retail local exchange customers, and that the RBOC will provide local exchange service only through ServeCo in competition with other CLECs.

65/ We recognize that some of the necessary deregulatory steps (for intrastate services) must be taken at the state level.

66/ The Commission has not yet addressed the regulatory treatment of RBOC bundled offerings, which therefore remain classified as dominant. *See Regulatory Treatment Order* at paras. 85-92. By "bundled" offerings, we mean selling both local and long distance at a single price, so that it is not possible to determine what the separate price for each service might be.

of a Section 272 affiliate should be treated as non-dominant, that decision rests on a foundation that is no longer valid. Specifically, the Commission's order relied in significant part on full implementation of its *Local Competition Order*, including those parts of the *Order* most necessary to permit RBOC competitors to use cost-based and efficiently provisioned UNEs in place of RBOC exchange access. However, key components of the *Local Competition Order* subsequently were invalidated by the Eighth Circuit, thereby invalidating the foundation for the Commission's previous ruling regarding regulation of RBOC interLATA services. ^{67/} Thus, an essential underpinning of the Commission's non-dominance decision is now missing, and the Commission will need to re-evaluate and reverse its decision accordingly. ^{68/}

For RBOCs that opt to implement the "Fast Track" structure, however, the Commission reasonably can, and should, declare that the ServeCo retail affiliate would be treated as a non-dominant carrier with respect to all its interstate retail offerings, including bundled packages that include local as well as interstate services. Dominant carrier regulation—which is primarily designed to prevent unreasonable discrimination, cross-subsidization, and other anti-competitive conduct—would be unnecessary if an RBOC were to adopt LCI's proposed structure. This is an additional important simplification of post-271 regulatory oversight for any RBOC which adopts LCI's "Fast Track" plan.

^{67/} See e.g., *Iowa Utilities Board v. FCC*, (Oct. 14, 1997 Order) (invalidating 47 C.F.R. § 51.315(b)); *Iowa Utilities Board v. FCC*, 120 F.3d 753, 793-800 (invalidating FCC's adoption of TELRIC providing standard for UNEs).

^{68/} For example, if the RBOC's interLATA affiliate purchases network elements from the RBOC to provide local exchange service, it may not be pricing that local service to cover the cost of the UNEs. In the absence of an independent fiduciary obligation in the affiliate, the affiliate is indifferent as to whether it covers the cost of inputs obtained from NetCo. In contrast, the ServeCo structure enhances prospects that ServeCo would accurately reflect the prices of inputs obtained from NetCo in its retail prices, and to insist that NetCo sell its inputs at cost, not at artificially inflated prices. As we also discussed above, the fact that the RBOC must charge the interLATA affiliate the same thing the RBOC charges others does not mean that those prices are real from the affiliate's point of view. See, e.g., 47 U.S.C. § 272(e)(3).

At the current time any exchange access services provided by an RBOC Section 272 affiliate still are considered dominant and regulated accordingly. This is appropriate given the regulatory problems discussed above. However, if the proposed ServeCo structure is adopted, the Commission can safely treat ServeCo's exchange access services as it would any other CLEC's. The Commission has declared that CLECs are non-dominant in their provision of exchange access, and has forbore from requiring CLECs to file tariffs for interstate exchange access.^{69/} Under the corporate structure we propose, it is appropriate to treat ServeCo in the same fashion.

CONCLUSION AND RULINGS REQUESTED

For the reasons set forth above, the Commission should issue the following declaratory rulings that would apply if an RBOC structures its operations so as to establish an independent "ServeCo" and otherwise comply with the conditions of LCI's "Fast Track" plan:

1. Section 271 and 272. When such RBOC submits an otherwise acceptable application for authorization to provide interLATA services originating in any in-region state, the RBOC shall receive a rebuttable presumption that it has met the competitive checklist provisions of Section 271(c)(2)(B) of the Act; that provision of interLATA service on this basis meets the requirements of Section 272 of the Act; and that the requested authorization is consistent with the public interest, convenience and necessity.

2. Section 251(h). A "ServeCo" created thereunder shall not be deemed a "successor or assign" of an ILEC for purposes of Section 251(h)(1)(B)(ii) of the Act, nor shall it be deemed a "comparable carrier" to an ILEC for purposes of Section 251(h)(2).

3. ServeCo Regulation. A "ServeCo" created thereunder shall be deemed a non-dominant carrier to the same extent as a CLEC that is not affiliated with an RBOC.

^{69/} See *Access Charge Reform Order* at paras. 359-64; *Hyperion Telecommunications, Inc. Petition Requesting Forbearance*, Memorandum Opinion and Order and Notice of Proposed Rulemaking, CCB/CPD Nos. 96-3 & 96-7 and CC Docket No. 97-146, 12 FCC Rcd 8596 (1997).

LCI urges the Commission to act expeditiously to grant these rulings, working with the relevant state commissions considering these matters, so that the current stalemate regarding local competition can be broken, with the benefits of full, robust competition for residential consumers.

Respectfully submitted,

LCI INTERNATIONAL TELECOM CORP.

By: 

Anne K. Bingaman
Douglas W. Kinkoph
LCI INTERNATIONAL TELECOM CORP.
8180 Greensboro Drive, Suite 800
McLean, VA 22102

Peter A. Rohrbach
Linda L. Oliver
HOGAN & HARTSON L.L.P.
Columbia Square
555 Thirteenth Street, NW
Washington, DC 20004

Rocky N. Unruh
MORGENSTEIN & JUBELIRER
One Market
Spear Street Tower, 32nd Floor
San Francisco, CA 94105

Eugene D. Cohen
326 West Granada Road
Phoenix, AZ 85003

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Its Counsel

CERTIFICATE OF SERVICE

I, Patricia A. Green, hereby certify that on this 22nd day of January, 1998, copies of the foregoing "Petition of LCI International Telecom Corp. for Expedited Declaratory Rulings" were served by hand on the following:


William E. Kennard, Esq.
Chairman
Federal Communications Commission
1919 M Street, N.W.
Room 814
Washington, D.C. 20554

Susan Ness, Esq.
Commissioner
Federal Communications Commission
1919 M Street, N.W.
Room 832
Washington, D.C. 20554

Harold Furchtgott-Roth, Esq.
Commissioner
Federal Communications Commission
1919 M Street, N.W.
Room 802
Washington, D.C. 20554

Michael K. Powell, Esq.
Commissioner
Federal Communications Commission
1919 M Street, N.W.
Room 844
Washington, D.C. 20554

Gloria Tristani, Esq.
Federal Communications Commission
1919 M Street, N.W.
Room 826
Washington, D.C. 20554


Patricia A. Green